



GOVERNING

Semiannual Report to Congress

April 1 – September 30, 2001

OIG

Office of Inspector General



BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM
WASHINGTON, D. C. 20551

OFFICE OF INSPECTOR GENERAL

October 31, 2001

The Honorable Alan Greenspan
Chairman
Board of Governors of the Federal Reserve System
Washington, DC 20551

Dear Chairman Greenspan:

The enclosed *Semiannual Report to Congress* summarizes the activities of the Office of Inspector General of the Board of Governors of the Federal Reserve System (Board) for the reporting period April 1 through September 30, 2001. During this reporting period, we continued to perform a variety of audits, reviews, investigations, and special projects that encompassed a number of legislative requirements and Inspector General community activities covering a wide range of the Board's programs and operations. Our accomplishments and work in progress are listed according to our strategic goals and objectives.

The Inspector General Act requires that you transmit this report to the appropriate committees of Congress within thirty days of receipt, together with a separate management report and any comments you wish to make.

Sincerely,

A handwritten signature in black ink, appearing to read "Barry R. Snyder", is positioned below the word "Sincerely,".

Barry R. Snyder
Inspector General

Enclosure



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April 1 – September 30, 2001

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Office of Inspector General

Table of Contents

	Page
Introduction	1
Goal 1: Provide Value-Added Customer Service to the Board.....	3
Goal 2: Enhance Coordination and Information Sharing.....	16
Goal 3: Enhance Internal Operations	21
Appendixes.....	25
Appendix 1—Audit Reports Issued with Questioned Costs for the Period April 1 through September 30, 2001	27
Appendix 2—Audit Reports Issued with Recommendations That Funds Be Put to Better Use for the Period April 1 through September 30, 2001	28
Appendix 3—OIG Audit Reports and Recommendations	29
Appendix 4—Cross-References to the Inspector General Act.....	30

Introduction

The mission of the Office of Inspector General (OIG), as prescribed by the Inspector General Act of 1978 (as amended), requires that we

- conduct and supervise independent and objective audits, investigations, and other reviews of Board programs and operations;
- promote economy, efficiency, and effectiveness within the Board;
- help prevent and detect fraud, waste, and mismanagement in the Board's programs and operations;
- review and make recommendations regarding possible improvements to existing and proposed legislation and regulations relating to Board programs and operations; and
- keep the Chairman and Congress fully and currently informed of problems.

Additionally, the Federal Deposit Insurance Act (as amended) requires us to review failed financial institutions supervised by the Board that result in a material loss to the bank insurance fund and produce, within six months of the loss, a report that includes suggestions for improving the Board's banking supervision practices. Further, through an agreement with other financial institutions regulatory agency Inspectors General charged with the same legislative requirement, we will address any relationship of Board-regulated holding companies to material losses to the fund from failed financial institutions supervised by any of these agencies.

The OIG currently performs its duties and responsibilities under four major program areas (as shown in the organizational chart that follows). Combined, these program areas perform traditional audits and investigations as well as some nontraditional consulting and partnering with Board management and staff.

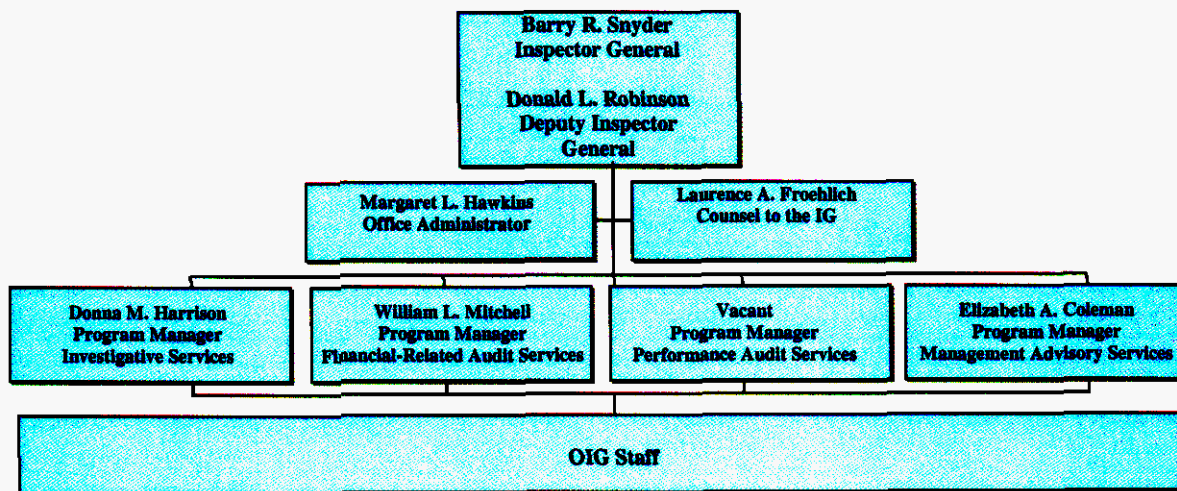
Our strategic plan for the period 2000 through 2004 includes the following three goals that guide our work:

- to provide value-added customer service to the Board;
- to enhance coordination and information sharing with the Congress, the IG community, and others; and
- to enhance the efficiency and effectiveness of our internal operations.

We are submitting our accomplishments and work in progress as they relate to these strategic goals and related objectives. Our statistical tables, as prescribed by the Inspector General Act, are shown in appendixes 1 through 4.

Office of Inspector General

September 2001



OIG Staffing	
Auditors	17
EDP Auditors.....	3
Investigators.....	4
Attorney	1
Administrative	2
Information Systems Analysts	2
Total Positions	29

Goal 1: Provide Value-Added Customer Service to the Board

Our first strategic goal focuses on providing value-added customer service to the Board. Our work within this goal focuses on the four strategic objectives that follow:

Improve and Enhance the Board's Program Operations

Over the next five years, the Board will continue to operate in a dynamic environment, shaped by legislative reform, increased emphasis on results and performance management, and innovations in the banking industry that require corresponding changes in the Board's supervision and regulation programs, as well as its Federal Reserve System (System) oversight functions. Within this environment, we are focusing on improving and enhancing Board programs and operations. Our work under this objective for this reporting period follows:

Audit of the Board's Efforts to Implement Performance Management Principles Consistent with the Results Act

The Government Performance and Results Act of 1993 (Results Act) was designed to ensure that federal agencies and the Congress have sufficient performance information to make important program and budget decisions. As stated in the Board's 1999 annual report, the Board is voluntarily complying with the requirements of the Results Act, although not required to do so. The Results Act requires the incorporation of the performance management concepts of strategic planning and performance measurement into agencies' planning and budgeting processes, and the issuance of plans and reports to the Congress.

We performed this audit to assess the current status of the Board's implementation efforts and to evaluate the benefits of fully integrating the Results Act concepts into the Board's planning and budgeting process. We found that the Board has not achieved its objective of voluntarily complying with the Results Act. Although the Board initially submitted required Results Act plans to the Congress on a timely basis, since July 1998, the Board has not finalized or submitted any required plans or reports. Additionally, while there are many positive aspects to its current planning and budgeting process, we believe the Board would benefit from an enhanced performance management culture that emphasizes obtaining and utilizing results-oriented information to manage its programs and functions and improving the accountability of staff.

Our report contained four recommendations designed to enhance the Board's current planning and budgeting process by developing a performance-management framework, as well as adding some key performance-management characteristics such as a longer-range planning horizon with a Boardwide planning focus, specific performance indicators and measures, and expanded

performance reports that show levels of achievement relative to the performance measures. Board management generally agreed with the intent of our recommendations and plans actions to address them. We will follow up on their implementation next year.

*Review of the Board's Oversight Approach for the
Modernization Project*

We completed our *Report on the Audit of the Board's Oversight Approach for the Federal Reserve's Check Modernization Project*. We initiated this audit in January 2001, because of the complexity, high cost, and importance of the check modernization project (project) and because the Director of the Division of Bank Operations and Payment Systems (RBOPS) requested an impartial assessment of the division's project oversight strategy. Our objective was to provide the Board with an independent and timely assessment of the effectiveness of RBOPS' oversight strategy so that any necessary adjustments could be made during the early stages of the project.

The Board approved the project in October 1999 to completely reengineer the Reserve Banks' check-processing infrastructure. The reengineering requires all Reserve Banks to adopt common software in order to create a nationwide system for processing checks, researching check-adjustment cases, archiving and retrieving check images, and delivering check services to depository institutions via the Internet. The project is expected to cost the Reserve Banks approximately \$93 million in capital outlays and \$242 million in additional operating expenses over a four-year period. The project is expected to directly impact 5,500 Federal Reserve System employees and over 8,000 customers. When completed, check processing will be standardized in all twelve Federal Reserve Districts.

In our report, we observed that RBOPS has implemented important elements of an appropriate and effective oversight strategy in the initial year of the project. Further, RBOPS has established an open environment for sharing project information and issues as they develop, primarily by providing liaisons to key committees and monitoring project reporting systems. We also observed that RBOPS had taken steps to ensure that staff involved in project oversight had designated backups.

We issued two recommendations that we believe will help RBOPS to focus its oversight strategy. We recommended that the director define a specific set of project oversight objectives that are linked to assessing how effectively project management is mitigating recognized project risks. We also recommended better integration of the results of work performed by General Auditors and RBOPS' reviews of General Auditor operations. The RBOPS' director agreed that these recommendations would strengthen the division's project oversight efforts and plans to implement them. Specifically, RBOPS has taken steps to refine and

focus its oversight strategy by developing a formal matrix to be shared with staff linking project oversight objectives to identified project risks. RBOPS also plans to incorporate the results of work performed by General Auditors and reviews of their work into key periodic reports and oversight planning meetings.

Review of the Board's Umbrella Supervision Program

We completed an audit scoping review of the Board's efforts to implement its umbrella supervision responsibilities as required by the Gramm-Leach-Bliley Act (GLBA). Enacted on November 12, 1999, the legislation, among other things,

- repealed core provisions of the Glass-Steagall Act and the Bank Holding Company Act that restricted bank holding companies from affiliating with securities firms and insurance companies;
- created a new corporate structure for financial service activities—the financial holding company (FHC);
- endorsed the concept of functional regulation, with continued primary oversight of individual legal entities by current functional regulators; and
- appointed the Board as the umbrella supervisor for all holding companies.

The objectives of our scoping review were to gauge the legislation's impact on the Board's financial institution supervision and examination program, and to assess progress made in implementing umbrella supervision.

To date, only one major securities broker dealer—Charles Schwab—has purchased a commercial bank; no FHC has acquired a large U. S.-based insurance company since the Citigroup-Travelers merger that predated GLBA; and only one large insurance underwriter—Metropolitan Life—has purchased a bank. Although approximately 500 institutions have opted for FHC status, three-quarters have assets of less than \$500 million, and half of these have assets of less than \$150 million. We believe the legislation's somewhat limited effect can also be traced to a pre-GLBA trend towards incremental financial modernization and the simultaneous evolution of supervisory approaches for handling larger and more complex organizations.

The Board has taken steps to develop its capacity to evaluate consolidated, entitywide risks posed by the largest institutions it supervises. Although GLBA provided little detail regarding how the new umbrella supervision responsibility should be fulfilled, the Board issued guidance that established a framework for coordinating FHC supervisory activities with the appropriate primary supervisors responsible for banking, insurance, and securities subsidiaries. Moreover, the umbrella supervision process has been crafted as an extension of the Board's

existing programs—the Bank Holding Company Inspection Program, and the risk-focused approach for examining large complex banking organizations.

The Board has also established initiatives that will assist in further developing its capability as umbrella supervisor. The Board created competency centers for economic capital and private equity merchant banking, a knowledge center for insurance, and supervisory specialty teams. These actions provide the System with focal points for training, knowledge transfer, and access to the specialized expertise necessary to supervise institutions that have opted for expanded financial activities.

Our scoping efforts have not identified any specific issues where immediate audit attention would add value. We will consider devoting resources in the future as the Board gains additional experience implementing umbrella supervision.

Strengthen and Streamline the Board's Operational Infrastructure

Over the next few years the Board faces certain challenges in ensuring that it has the people, processes, and technology that it will need to meet the evolving and varying needs of its clients and to provide a wide range of high-quality services in a cost-effective manner. To be effective, the Board will need to reexamine its financial management, human capital, administrative operations, and communications infrastructure with a view toward improving operations and strengthening accountability. We will provide value-added services to help Board management ensure that it has the integrated internal systems, policies, and processes it needs to meet these new demands. Our work under this objective during this reporting period follows:

Finance Function Assessment

In coordination with the Board's Staff Director for Management and the Associate Director for the Management Division's Finance Function, we initiated an assessment of the Board's finance function. The project objectives are to (1) assess the operations of the finance and accounting function and the level of controls needed to meet business objectives, and (2) determine whether the current organizational strategy and structure support the goal of providing accurate, responsive, and high quality service. To accomplish our objectives, we are blending analytical techniques typically used in program auditing, collaborative assurance engagements, and business process reviews. Our assessment framework includes an analysis of financial-related objectives and risks, critical processes, systems, documentation, and performance measures.

During this period, we reported on the initial phase of this project which, at the Staff Director's request, focused on the Board's position management process. Our objectives were to assess the risks and internal control framework associated with the position management function and determine whether the current workflow process is appropriately balanced from a risk-focused perspective. To accomplish these objectives, we conducted facilitated sessions with staff and managers in the Finance Function, Human Resources Function (HR), and client divisions. We also prepared detailed flowcharts to assess position management internal controls and workflow processes. Our analysis focused on the risks and controls associated with organizational changes that do not affect a division's total number of authorized positions or net dollars.

In summary, we reported that the Board's current process for evaluating organizational changes that exceed a division's total authorized positions appear to be congruent with budget control policies and practices used in private and public sector organizations. At the same time, our analysis showed opportunities to eliminate duplication of effort and excessive control by streamlining the approval process for organizational changes that are within a division's authorized budget and position levels. We tested one of the most complex scenarios in this category and found that a process that now involves ten handoffs and ten approvals could be reduced to four handoffs and three approvals without exposing the Board to additional risk. We believe that streamlining the process is possible because risks associated with position changes that do not exceed budget authority are mitigated by controls that are already embedded in the responsibilities assigned to HR. The action items presented to the Staff Director highlighted the need for simplifying the position management workflow process and enhancing coordination between Finance Function and HR staff.

Work on the remainder of our assessment will continue into the next reporting period.

Review of the New Building Acquisition

In 2000, Congress passed legislation amending section 10 of the Federal Reserve Act authorizing the Board to acquire a new building to provide for the performance of the functions of the Board. This acquisition represents a major undertaking for the Board. During the reporting period, we started a monitoring effort related to the acquisition's planning, contract solicitation, and approval processes. Similar to our monitoring effort related to the Eccles Building Infrastructure Enhancement Project, we reviewed the overall project management and internal controls and provided informal feedback on our observations.

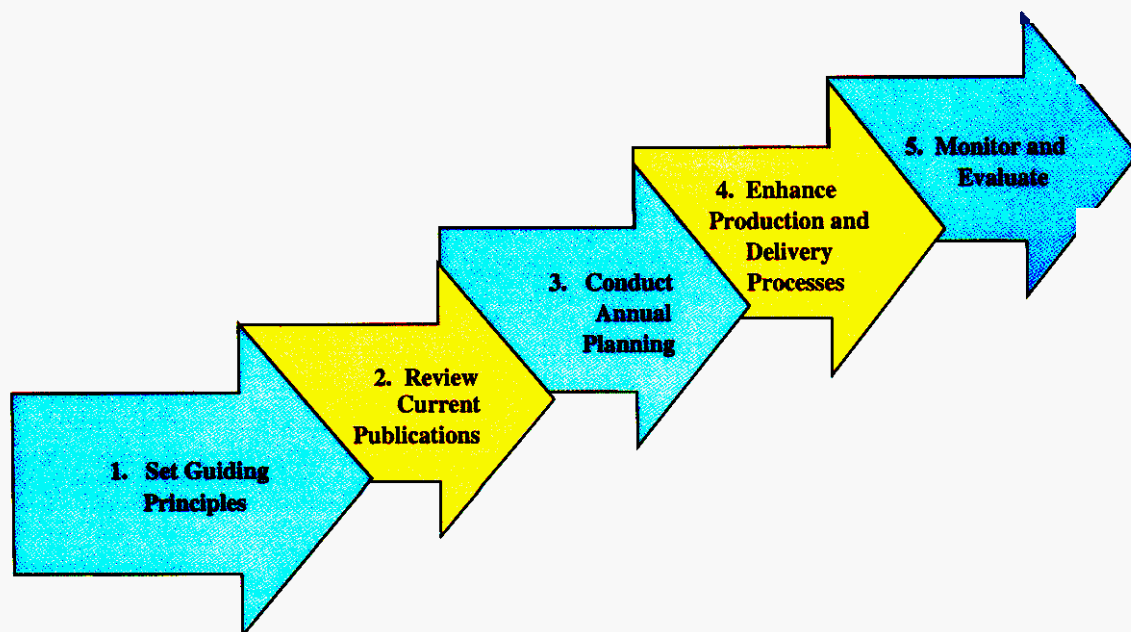
In September 2001, the Board signed a contract acquiring the building at 1709 New York Avenue. The Board had been leasing over 70 percent of the building and the Board's lease-purchase analysis showed that the acquisition will reduce

costs in the long run. During the project's various phases, we did not identify any issues requiring management's attention and we have closed our monitoring efforts related to this project.

Phase II of the Business Process Review of the Board's Publications Program

On the second phase of this business process review, we continue to coordinate with the Board's Publications Committee (committee) as it transitions the Board's publications program from a publications-based approach to an information-based communications approach that more fully optimizes the advantages of the Internet and electronic media. The publications program supports the Board's missions by making information about the Federal Reserve accessible to the federal government, regulated entities, legal and business communities, libraries and research entities, economists and other scholars, consumers, and the public at large. The committee, composed of senior officials from several Board divisions and offices, oversees the program. As a result of our phase one work, the committee adopted a five-step approach designed to help the Board streamline processing, promote efficient operations, improve performance, implement best practices, and optimize the use of technology in its publications program. During the prior reporting period, the committee focused on the first step in completing the transition to an information-based communications approach—developing principles to guide decisions by those Board divisions and offices that are primarily responsible for determining the information that should be communicated to the public.

Steps to Developing an Information-Based Communications Program



During this period, we assisted the committee chair as she worked with the publication owners to implement transition step two—performing zero-based reviews of current publications in the context of the guiding principles. Specifically, we

- provided additional data regarding potential savings associated with modifying the *Federal Reserve Bulletin*, in support of the committee’s review of this publication;
- participated in a briefing to Division of Banking Supervision and Regulation (BS&R) officials to facilitate their zero based review of various manuals; and
- reviewed the approach that we used during the publications review to survey readers of the *Federal Reserve Bulletin* to assist the committee in preparing its Paperwork Reduction Act justification which, upon approval, will enable Board staff to conduct any surveys of publication users that might be needed over the next three years.

We also provided the committee chair with a report that provides our observations, suggestions, and supporting rationale for implementing various degrees of organizational change for publication-related activities—information that will be useful in developing the Board’s 2002-03 budget. At the committee chair’s request, we are also preparing a white paper to facilitate the committee’s zero-based review of the Board’s annual report and annual report budget review.

Promote the Board’s Effective Use of Technology

Information technology continues to advance at a rapid pace, requiring the Board to continually balance automation requirements and costs with service delivery, efficiency, and security concerns. While Board divisions and offices have made significant progress in integrating information technology into their work, a more fully integrated information technology infrastructure would provide enhanced support to the Board in achieving its mission-related, strategic planning, human capital, and business process objectives. Our work under this objective for this reporting period follows:

Audit of the Board’s Information Security Program

On October 30, 2000, the President signed into law the FY2001 Defense Authorization Act, including Title X, subtitle G, “Government Information Security Reform” (Security Act). The Security Act amends the Paperwork Reduction Act of 1995 (PRA) by enacting a new subchapter on “Information Security” and provides a comprehensive framework to ensure proper management and security of information resources supporting federal operations and assets.

The Security Act codifies existing information security requirements found in Office of Management and Budget Circular A-130, Appendix III, and reiterates security responsibilities outlined in other legislation, including the Computer Security Act of 1987, PRA, and the Clinger-Cohen Act of 1996.

The Security Act also requires each agency Inspector General to conduct an annual independent evaluation of the agency's information security program and practices. This was the first year that such evaluations were required; similar evaluations are to be conducted next year with Congress to make a judgment as to whether they will be required thereafter. Our specific audit objectives, based on Security Act requirements, were to evaluate the effectiveness of security controls and techniques for selected information systems and to evaluate the Board's compliance with the Security Act and related informational security policies, procedures, standards, and guidelines.

Overall, we found that the Board's information security program is generally effective. Our security control tests did not identify any major security control weaknesses, although we found that controls needed to be strengthened in several areas. We provided our test results to management under separate restricted cover and we plan to follow up on implementation of our recommendations as part of future audit activities related to the Board's implementation of the Security Act.

Although the Board's information security program is generally effective, we found that the Board has not yet achieved full compliance with Security Act requirements. The Board follows the guidance contained in the System's *Information Security Manual (ISM)*, which contains a fairly comprehensive set of general guidelines regarding information security. While we found that the majority of Security Act requirements were covered in the ISM, several key aspects of the Security Act were either not addressed or were addressed to a limited extent. Specific areas where we believe additional guidance is required are: clearly defining roles and responsibilities; developing security plans; enhancing annual security control reviews; and responding to security-related incidents. We also believe additional opportunities exist to enhance the Board's information security program relating to security awareness and training and to the risk assessment process.

Our report contains seven recommendations designed to help bring the Board into compliance with the Security Act and enhance the Board's information security program. The Staff Director for Management generally agreed with our recommendations and has identified actions to address them. We will follow up on the Board's implementation of our recommendations as part of our future audit work pertaining to the Security Act.

Supervisory Information Technology Partnership

The Supervisory Information Technology (SIT) Section of BS&R provides information technology management services for the supervision function. In response to their request, we established an ongoing liaison with SIT management and staff to serve as a sounding board as they pursue their strategy over the next year. During this reporting period, we continued to monitor SIT's work on business application and infrastructure projects, as well as products that support field work in all supervision areas. SIT is committed to helping ensure that formal project management processes and established standards guide new information technology initiatives.

Going forward, we plan to provide our views, in an advisory capacity, on the further development and implementation of the Banking Organization National Desktop (BOND) application, from both a technical and user perspective. BOND is intended to facilitate real-time, secure information sharing and collaboration across the System and with certain other federal and state regulators to support the risk-focused supervision of large, complex banking organizations. Our participation will give us a practical understanding of the application development approach.

Follow-up of the Division of Reserve Bank Operations and Payment Systems' Distributed Processing Environment

During the reporting period, we continued follow-up work related to our March 1998 *Report on the Audit of the Division of Reserve Bank Operations and Payment Systems' Distributed Processing Environment*. Our previous follow-up efforts resulted in closing two of the three audit recommendations. Earlier this year, RBOPS revised its continuity of operations plan as part of a Boardwide planning effort. Based on our review of the division's plan, we have closed our third, and final, recommendation related to contingency planning.

Help the Board Limit Risk and Ensure Compliance

The Board operates under a myriad of laws and regulations that impact many aspects of its programs and operations. For example, numerous tax and employment laws and regulations impact the Board's recruiting, compensation, and benefits programs. In addition, Board programs and operations may also be subject to potential damage or loss through fraud, waste, abuse, mismanagement, and employee misconduct. Our work under this object for this reporting period follows:

Audit of the Federal Reserve's Background Investigation Process

Earlier this year, the U.S. House of Representatives Committee on Financial Services, Subcommittee on Oversight and Investigations, requested that the OIG perform a review of the Board's background investigation process. The subcommittee is concerned that sensitive and private financial data utilized by federal financial regulatory agencies could be improperly accessed, used, or manipulated.

Our specific audit objective, based on the subcommittee's request, was to evaluate the policies, procedures, and practices under which the Board conducts, adjudicates, and documents background investigations of prospective and current employees and contractor personnel. Because Reserve Bank personnel participating in the Board's delegated supervision and regulation program also have access to financial data, we included them in our audit scope.

During this reporting period, we completed our fieldwork, discussed our findings and recommendations with management, and issued our draft report to the Staff Director for Management for comment. Our fieldwork included a review of personnel files for all current Board employees, a similar review for a judgmental sample at two Reserve Banks, and a review of a judgmental sample of contracts at the Board. During the next reporting period, we will finalize our report, which will include the Staff Director's response.

Audit of the Board's Government Travel Card Program

In December 2000, we began an audit of the Board's Government Travel Card (GTC) program. Our audit objectives were to evaluate the goals and objectives of the GTC program and determine whether they are being achieved in an efficient and effective manner; assess whether control procedures are sufficient; determine whether control procedures are adequate to ensure proper use of the GTC; and evaluate program compliance with applicable laws and regulations. We completed our fieldwork and have provided a draft report to management for comment. We will summarize our audit findings, conclusions, and recommendations in the next semiannual report.

Audit of the Board's Use of and Controls over Purchase Cards

The OIG recently began an audit of the use of and controls over purchase cards. We began this audit based on reports identifying specific control weaknesses leading to unauthorized purchases and misuse of purchase cards at other government agencies during the past year, and as a follow-on effort to our audit of the travel credit card program. Our objective for the audit is to assess the adequacy of the existing internal controls over the Board's purchase card

program. Specifically, we plan to evaluate existing purchase card program goals and objectives; determine the adequacy of procedures for issuing cards and ensuring proper use; and evaluate employees' compliance with current Board policy. We will complete this audit during the next reporting period and present our findings and conclusions in the next semiannual report.

Follow-up of the Academic Assistance Audit

We completed a follow-up of our *Report on the Audit of the Board's Academic Assistance Program*. The audit report contained ten recommendations for improving the internal controls of the Board's academic assistance program. During our follow-up, we found that sufficient actions have been taken to close all of the recommendations.

Investigative Activity

During the reporting period, we opened seven formal investigations and continued work on twenty-three cases that were opened during previous reporting periods. Of the thirty active cases, we closed two cases that were opened from the previous reporting periods. The first case required a legal determination of the facts involving either an employee's alleged unauthorized use of Board property or their receipt of a gift from a prohibited source. It was referred to the Board's General Counsel and the Designated Agency Ethics Official. The employee subsequently entered into a settlement agreement with the Board involving a separate matter, thus resolving further agency action associated with misconduct in this case. The second case involved the alleged frequent flyer abuse by a Board employee in which the use of personal miles earned on official business were paid for by a third party, not the Board. In this second case, the Board's Legal Division advised us that because the scope of the law and the Board's travel policy in effect at the time of occurrence were insufficiently clear, frequent flyer miles obtained as the result of airline tickets paid for by a third party may have been allowable as personal miles by the Board employees. As a result of our work, we recommended that the Board amend its travel policy to provide more guidance regarding the use of frequent flyer awards obtained in connection with official travel when the travel is paid for by a nongovernmental source.

In addition to the two investigations closed during the previous reporting period, we closed three cases that were opened during this reporting period. One involved the alleged theft of government money in excess of \$8,000 by a former employee and required the OIG to refer it to the local prosecutor to determine whether it merited criminal prosecution. The U.S. Attorney's Office declined prosecution in favor of administrative action. The second investigation involved a former employee's alleged theft of Board computer equipment and resulted in a conviction of theft-related offenses. The subject admitted to removing, without

permission, three laptop computers from the Board. The subject sold at least one of the computers to a pawnshop in Montgomery County, Maryland. As a result of the OIG investigation, the subject's employment was terminated and the Board increased its internal controls of computer equipment. The subject entered a guilty plea to theft in the District of Columbia Superior Court and was sentenced to eighteen months supervised probation, 400 hours of community service, and was required to pay \$150 to the Victims of Crime fund, and a \$250 fine. The subject also pled guilty to one count of theft in the District Court of Maryland for Montgomery County and was sentenced to prison (suspended), eighteen months supervised probation to be served concurrent with the sentence in the District of Columbia. We were assisted during our investigation by the Metropolitan Police Department, Washington, DC, the Takoma Park Police Department, and the ISB/Pawn Unit, Montgomery County, Maryland. The OIG received prosecutorial assistance from the office of the U.S. Attorney for the District of Columbia, and from the office of the Maryland States Attorney for Montgomery County. The third case closed during this reporting period involved an alleged identity theft and suitability for employment matter on the part of a Board employee. During OIG's investigation, the employee resigned from their position.

The investigative findings in four of our active cases involved alleged frequent flyer abuse by Board employees and required the OIG to refer them to the local prosecutor to determine whether they merited criminal prosecution. The U. S. Attorney's Office declined prosecution of all four investigations in favor of administrative action. Although the Board has updated its travel policy to provide more guidance regarding the accumulation and use of frequent flyer awards, to date, it has not taken any administrative action in these four cases, or the twelve other frequent flyer cases previously referred to them during earlier reporting periods. At the end of this reporting period, we had twenty-five active cases. Our summary statistics on investigations are provided in the table that follows:

Summary Statistics on Investigations for the Period of April 1 through September 30, 2001

Investigative Actions	Number
Investigative Caseload	
Investigations Opened during Reporting Period	7
Investigations Open from Previous Period	23
Investigations Closed during Reporting Period	5
Total Investigations Active at End of Reporting Period	25
Investigative Results for this Period	
Referred to Prosecutor	5
Referred for Audit	0
Referred for Administrative Action	6
Oral and/or Written Reprimand	0
Terminations of Employment	1
Demotion	0
Suspensions	0
Debarments	0
Indictments	1
Convictions	1
Monetary Recoveries	\$0
Civil Actions (Fines and Restitution)	\$0
Criminal Fines: Fines & Restitution	\$525

Goal 2: Enhance Coordination and Information Sharing with the Congress, IG Community and Others

To achieve our mission, we will need to work closely with Board management, the General Auditors at the Reserve Banks, the Congress, the Inspector General community, and other stakeholders. We plan to continue and expand our coordination with Inspectors General at the financial regulatory agencies to promote consistency in evaluations and priorities and with the IG community across the federal government to provide more global assessments of issues. We will strive to take full advantage of technology and innovative reporting and communications vehicles to enhance information sharing with our diverse stakeholders.

Develop and Enhance Relations with the Congress

By law, the OIG has a duty and responsibility to keep Congress fully and currently informed by means of semiannual and other reports concerning fraud and other serious problems, abuses, and deficiencies relating to the administration of programs and operations administered or financed by the Board, recommend corrective actions concerning such problems, abuses, and deficiencies, and report on the progress made in implementing corrective actions. With the U. S. General Accounting Office increasing its attention on the many broad and more global issues facing the government, we believe we will have a greater responsibility to identify and address current and emerging issues related to Board programs and operations that are of high importance to Congress. Our work under this objective for this reporting period follows:

Review of Legislation and Regulations

To achieve this objective, we review existing and proposed legislative and regulatory items both as part of our routine activities and on an *ad hoc* basis. We routinely keep track of proposed and pending legislation and regulations by researching documents and databases relevant to legislative and regulatory matters, reviewing lists prepared by the Board's law library, sharing information with others in the Inspector General community, and coordinating with Board programs that also review new and proposed legislation. We then independently analyze the effect that the new or proposed legislation or regulation may have on the efficiency and effectiveness of Board programs and operations. We also conduct reviews of proposed agency directives in order to suggest revisions that will improve the effectiveness of such internal regulations.

During this period, we reviewed a number of legislative proposals for their potential impact on either the Board or on the Office of Inspector General, and provided advice as appropriate. We also reviewed and provided substantive

comments on the Board's draft policy and procedure relating to the "Use of Nonpublic Personnel Information," a document designed to enhance the privacy protections afforded to sensitive information about Board employees. A number of our suggestions were incorporated into the final policy statement. We also provided comments to the Office of Management and Budget on its draft "Guidance for Preparing and Submitting Security Plans of Action and Milestones" under the Government Information and Security Reform Act.

As part of our support to ongoing Board projects, we finished a comprehensive review of federal employment laws to determine whether and how they apply to the Board's human resources programs and benefits. The information is being incorporated into a prototype database that will serve as a research tool to facilitate data retrieval and analysis from a variety of perspectives. Finally, we completed a comprehensive U.S. General Accounting Office (GAO) survey designed to elicit views from the Inspector General community on the advantages and disadvantages associated with organizational and operational changes that are under consideration by the House Committee on Government Reform. Consolidating IG offices either by moving smaller offices into larger offices or by combining several IGs into a new office is one of the more significant issues under review, and GAO indicates that the survey results will be critical in developing their conclusions and recommendations to the committee.

Improve Our Responsiveness to All Allegations of Fraud, Waste, Abuse, or Mismanagement and to the Public Requests for Information

We are continuing to look for opportunities to improve our timeliness to Board management and staff, Congressional staff, and others concerning allegations of wrongdoing and to enhance our communications with the general public regarding their potential concerns with the Board's programs and operations and their need for information. Our work under this objective during this reporting period follows:

Hotline Operations

Our investigators continued to address allegations of wrongdoing related to the Board's programs and operations, as well as violations of the Board's standards of conduct. During this reporting period, we received 151 complaints, of which 143 were from our hotline operation. Most hotline callers were consumers with complaints or questions about practices of private financial institutions. Those inquiries involved matters such as funds availability, account fees and charges, and accuracy and availability of account records. We continued to receive numerous questions concerning how to process Treasury securities and savings bonds. Other callers contacted us seeking advice about programs and operations

of the Board, Federal Reserve Banks, other OIGs, and other financial regulatory agencies. OIG investigators directed those inquiries to the appropriate Board offices, Banks, or federal or state agencies. We closed all of the 143 hotline complaints after our initial analysis and contact with the complainants.

In addition to the hotline complaints, the investigative services program received eight allegations that were referred to the OIG from Board program staff, OIG audit activities, and other sources. As a result of those allegations, the OIG opened seven investigations. In addition, we are continuing our review of fictitious instrument fraud complaints. Fictitious instrument fraud schemes are those in which promoters promise very high profits based on fictitious instruments they claim are issued, endorsed, or authorized by the System or a well-known financial institution. Our summary statistics of the hotline results are provided in the table that follows:

Summary Statistics on Hotline Results for the Period of April 1 through September 30, 2001

Investigative Actions	Number
Complaints Referred for Investigation	
Hotline Referrals	143
Audit Referrals	0
Referrals from Other Board Offices	7
Referrals from Other Sources	1
Proactive Efforts by OIG	
Investigations Developed by OIG	0
Results of all Complaints Referred and Proactive Efforts	
Resolved	143
Pending	8
Total Received during Reporting Period	151

Web Page Development and Enhancement

The OIG web site has become the primary method of disseminating information to the System, as well as to the general public, regarding our operations. It is designed to show our accomplishments and our future direction, and allow visitors to know who we are, what we do, and how to contact us. We recently completed a redesign of our web site as part of a multiphased strategy to provide additional functionality and enhanced information content. We believe that the new design is more dynamic while affording the user an easier means of finding information for each of our ongoing projects and a centralized OIG reading room

containing links to our reports and planning documents. It is our goal to keep this site up to date. We plan regular enhancements as we integrate the site with our other business processes.

Take a Positive Leadership Role in the IG Community

While our primary mission is to enhance Board programs and operations, we are also members of the broader IG community. Executive Order 12805 established the President's Council on Integrity and Efficiency (PCIE) and the Executive Council on Integrity and Efficiency (ECIE). The PCIE is primarily composed of Presidentially appointed IGs, while the ECIE is composed of statutory IGs of designated federal entities. The order directs the councils to continually identify, review, and discuss areas of weakness and vulnerability to fraud, waste, and abuse, in federal programs and operations, and to develop plans for coordinated, governmentwide activities that address these problems and promote economy and efficiency. In addition, the community strives to address a number of common environmental factors, such as auditor and investigator training, OIG operations, management issues, and legislative changes. Our work under this objective during this period follows:

Executive Council on Integrity and Efficiency Participation

As Vice Chair of the Executive Council on Integrity and Efficiency (ECIE), the Board's Inspector General provides leadership, vision, direction, and initiatives for the ECIE on behalf of the Council Chair (Deputy Director for Management, Office of Management and Budget). The Inspector General also was recently named to the Comptroller General's Advisory Council *on Government Auditing Standards* (Yellow Book), a twenty-member group that works with the General Accounting Office to keep the auditing standards current through the issuance of revisions and guidance. Through our membership on these councils and other groups, we participate in, and set the direction for, a wide range of initiatives. During this reporting period, for example, the ECIE joined the President's Council on Integrity and Efficiency (PCIE) in developing and adopting *A Strategic Framework* to guide their work over the next three years. Within this framework, the ECIE is focusing on strategies to enhance its effectiveness in addressing mission-related challenges at the agencies it oversees, placing increased emphasis on building interagency alliances to address common concerns, networking with peers throughout the OIG community, and reaching out to congressional leaders to keep them informed on our work.

Foster Interagency Approaches to Cross-Cutting Issues

As noted earlier, major economic, financial, and social trends (such as market globalization, technological and financial innovations, and statutory and regulatory framework revisions) will shape the environment in which the Board and the other financial regulatory agencies operate. These factors will also affect the strategic direction of the regulatory OIGs and require creative and innovative approaches to providing their respective agencies with assistance in managing change, maximizing the use of scarce resources, and ensuring continued compliance with applicable laws and regulations. Our work under this objective during this reporting period follows:

IG Community Participation

Through our membership and leadership role in the ECIE and our continued participation in the Council of Counsels to the Inspectors General, we helped set the direction of interagency projects—including audits, inspections, and investigations. We also maintained communications with groups such as the Government Performance and Results Act Coordinators' Interest Group and the PCIE/ECIE Working Group on critical infrastructure assurance that helped us to share review techniques and offer OIG staff the opportunity to network with peers throughout the IG community.

Goal 3: Enhance the Efficiency and Effectiveness of Internal Operations

We plan to continually review our own processes, systems, and resources in an effort to improve our service delivery and to serve as an efficient and effective organization within the Board. Specifically, we plan to improve and streamline our major business processes, continue our investment in human capital, and focus on management approaches to produce the results envisioned in our strategic plan.

Continue to Improve Our Business Processes

Through the effective use of information technology and numerous process enhancements, we have made significant improvements in the way we perform our audits, investigations, and other projects. However, future technological innovations will provide additional opportunities for improvement. Our work under this objective for this reporting period follows:

Lotus Notes Migration

We began this effort as part of our migration strategy to a standardized Notes domain structure throughout the Federal Reserve System. This project represents the single largest internal project during the past several months and included conversion of all user mail accounts as well as all internal Notes applications. We have completed the mail portion of the migration and have reviewed all internal applications and revised coding as required. As part of our migration strategy, we also acquired a new application server and brought it online earlier this year. During the fourth quarter of 2001, we will complete user testing of our primary applications in the new domain and finish the migration process.

Financial Statement Audit Contract

The OIG contracts for the independent public accounting firm's audit of the financial statements of the Board and the Federal Financial Institutions Examination Council (FFIEC). (The Board performs the accounting function for the FFIEC.) Our auditors plan and perform the work necessary to obtain reasonable assurance that the financial statements are free of material misstatement. The audits include examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. The audits also include an assessment of the accounting principles used and significant estimates made by management, an evaluation of the overall presentation of the financial statements, and a review of the internal controls over financial operations and reporting.

The audit of the 2000 financial statements, completed earlier this year, was the final option year on our prior contract. During the past several months, we

worked closely with the Board's procurement staff to award a financial statement audit contract for the 2001 financial statements and beyond. We prepared the necessary solicitation documents, evaluated bids received, and awarded a contract at the end of September. KPMG LLP was the successful bidder and we will begin planning activities with the new auditors later this year for the audit covering the 2001 financial statements.

Enhance Our Human Capital Through Effective Leadership and Management of Our Staff

Human capital is the fundamental building block to achieving an organization's mission and goal's, and we have integrated human capital considerations in developing our vision and values, goals and objectives, and the strategies to achieve them. Enhancing our human capital will be one of our highest priorities over the next several years. The major objectives are to

- provide opportunities for staff to do different and challenging work;
- expand the staff's opportunities to learn and apply their knowledge and abilities;
- expand staff's career choices, career paths, job enrichment options, and career opportunities;
- allow staff to take responsibility for managing their developmental goals and career options;
- produce experts of the Board's business and in the OIG's mission that will create best solutions for addressing issues and problems impacting the Board's programs and operations;
- allow the OIG to assemble, integrate, and retain highly talented employees who stay at the forefront of their professions;
- make it easier for OIG managers to coach, provide feedback, and develop the staff required to accomplish current and future business strategies; and
- improve the quality of performance and career development discussions between managers and employees.

Our work under this objective for the reporting period follows:

New Hire Orientation

We established a New Hire Orientation task force to upgrade and standardize the way in which the OIG introduces new employees to the work environment and work processes. The objective is to design a program to introduce new staff to office policies, pertinent administrative matters, and technical issues, and, provide continued mentoring support. During this reporting period, the task force prepared an orientation handbook for new OIG staff members.

Individual Development Plan

We are continuing our process to create individual development plans (IDP) for each OIG staff member as part of our strategic approach of emphasizing career development and professional growth. The IDPs are being designed to identify the core knowledge, skills, abilities, and behaviors needed to achieve our mission and strategic direction, and enhance our staff's talents where required.

During this period, we focused our efforts on the OIG manager positions and refined and grouped our core competencies in the following categories:

- Analytical/Technical Skills
- Knowledge and Experience
- Leadership and Management Abilities
- Personal Characteristics
- Interpersonal Skills

We also finalized our IDP form and developed a methodology for manager's and staff to follow during the process. To implement the process, we developed a skills assessment checklist, drafted a developmental opportunities guide and formatted a resume summary for staff to document their achievements. We plan to begin using our new process during the next reporting period.

Appendixes

Appendix 1

Audit Reports Issued with Questioned Costs for the Period April 1 through September 30, 2001

Reports	Number	Dollar Value	
		Questioned Costs	Unsupported
For which no management decision had been made by the commencement of the reporting period	0	\$0	\$0
That were issued during the reporting period	0	\$0	\$0
For which a management decision was made during the reporting period	0	\$0	\$0
(i) dollar value of disallowed costs	0	\$0	—
(ii) dollar value of costs not disallowed		—	—
For which no management decision had been made by the end of the reporting period	0	\$0	\$0
For which no management decision was made within six months of issuance	0	\$0	\$0

Appendix 2

Audit Reports Issued with Recommendations That Funds be Put to Better Use for the Period April 1 through September 30, 2001

Reports	Number	Dollar Value
For which no management decision had been made by the commencement of the reporting period	1	\$29,070
That were issued during the reporting period	0	\$0
For which a management decision was made during the reporting period	0	\$29,070
(i) dollar value of recommendations that were agreed to by management	—	\$29,070
(ii) dollar value of recommendations that were agreed to by management		—
For which no management decision had been made by the end of the reporting period	1	\$0
For which no management decision was made within six months of issuance	1	\$0

Appendix 3

OIG Audit Reports With Outstanding Recommendations

Report No.	Audits Currently Being Tracked	Issue Date	Recommendations			Status of Recommendations ¹		
			No.	Mgmt. Agrees	Mgmt. Disagrees	Follow-up Completion Date	Closed	Open
Monetary and Economic Policy								
None currently being tracked								
Supervision and Regulation of Financial Institutions								
A9508	Audit of the Board's Consumer Compliance Examination Process	04/96	14	11	3	10/99	12	2
A9610	Audit of the Division of Banking Supervision and Regulation's Distributed Processing	06/97	5	5	0	08/98	2	3
A9710	Audit of the Federal Reserve System's Application Commitment Processing	01/98	5	5	0	06/99	4	1
A9810	Audit of the Board's Supervisory Process for Implementing the Community Reinvestment Act	03/99	8	7	1	09/00	5	3
Oversight of Federal Reserve Bank Activities								
A9707	Audit of the Division of Reserve Bank Operations and Payments Systems' Distributed Processing Environment	03/98	3	3	0	08/01	3	0
A0013	Audit of the Board's Oversight Approach for the Federal Reserve's Check Modernization Project	09/01	2	2	0			
Federal Reserve Board Administrative Operations								
A9702	Business Process Review of the Board's Travel Administration	07/97	9	9	0	01/99	1	8
A9811	Audit of the Board's Academic Assistance Program	02/99	10	10	0	06/01	10	0
A9903	Review of the Board's Frequent Flyer Policy	06/00	2	2	0	—	—	—
A0002	Review of the Board's Implementation of Critical Infrastructure Protection	09/00	3	3	0			
A004	Audit of the Board's Efforts to Implement Performance Management Principles Consistent with the Results Act	07/01	4	4	0			
A0106	Audit of the Board's Information Security Program	09/01	7	7	0	—	—	

¹ A recommendation is closed if (1) the corrective action has been taken; (2) the recommendation is no longer applicable, or (3) the appropriate oversight committee or administrator has determined, after reviewing the position of the OIG and division management, that no further action by the Board is warranted. A recommendation is open if (1) division management agrees with the recommendation and is in the process of taking corrective action or (2) division management disagrees with the recommendation and we have referred it to the appropriate oversight committee or administrator for a final decision.

Appendix 4

Cross-References to the Inspector General Act

Indexed below are the reporting requirements prescribed by the Inspector General Act of 1978, as amended, for the reporting period:

Section	Source	Page(s)
4(a)(2)	Reviews of legislation and regulations	16
5(a)(1)	Significant problems, abuses, and deficiencies	None
5(a)(2)	Recommendations with respect to significant problems	None
5(a)(3)	Significant recommendations described in previous Semiannual Reports on which corrective action has not been completed	None
5(a)(4)	Matters referred to prosecutory authorities	15
5(a)(5)	Summary of instances where information was refused	None
5(a)(6)	List of audit reports	3-13
5(a)(7)	Summary of significant reports	None
5(a)(8)	Statistical Table—Questioned Costs	27
5(a)(9)	Statistical Table—Recommendations that Funds Be Put to Better Use	28
5(a)(10)	Summary of audit reports issued before the commencement of the reporting period for which no management decision has been made	29
5(a)(11)	Significant revised management decisions made during the reporting period	None
5(a)(12)	Significant management decisions with which the Inspector General is in disagreement	None



Inspector General Hotline

1-202-452-6400

1-800-827-3340

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You may also write the:

Office of Inspector General

HOTLINE

Mail Stop 300

Board of Governors of the Federal Reserve System

Washington, DC 20551